

Congress of the United States
CONGRESSIONAL OVERSIGHT PANEL

Opening Statement of Kenneth Troske

Congressional Oversight Panel Hearing on the TARP and Executive Compensation Restrictions

October 21, 2010

Thank you, Chairman Kaufman.

I would like to start by thanking all of the witnesses for appearing before the panel today. I recognize that all of you are very busy people with a number of other responsibilities, so I appreciate you taking time to travel here and help us with our oversight responsibilities.

As we are all aware, the issue before us today—examining the government’s efforts to regulate how firms compensate executives—remains one of the more controversial issues to arise out of the recent financial crisis. Taxpayers remain incensed about the large bonuses received by executives at firms that received enormous government bailouts. Much of the recent discussion of executive compensation has focused on several issues: should executives of bailed out financial firms receive bonuses; do bonuses cause managers to focus on short-term gains as opposed to the long-term growth of a company; and have boards of directors of large financial firms been captured by management so that they simply rubber stamp managerial decisions instead of engaging in the appropriate amount of oversight? While I recognize that there can be instances in which the way firms compensate executives is not always perfectly in line with the interests of shareholders, I believe that the market can and will correct most inefficiencies. However, in my opinion the fact that for the past forty years the Federal Government has made it clear that it would use taxpayer money to insure large financial firms against failure creates a distortion that actually exacerbates the problems mentioned above. This means that if we could simply get rid of the government guarantee that has created “too big to fail firms,” then many if not most of these problems would largely disappear. It also means that by focusing on these ancillary problems we fail to fix the true problem that is producing so much anger.

In regards to the specific issue of executive compensation, recent research from the Federal Reserve Bank of Minneapolis shows that, in almost every setting, shareholders of firms will choose to pay workers in an efficient manner. In other words, workers will be paid in a way that maximizes shareholder wealth without imposing costs on the rest of society. The one exception to this rule is when the government provides an implicit or explicit guarantee of the firm’s debt and does not charge the firm for this guarantee. In this case shareholders will chose to incentivize workers in ways that encourage them to take an excessive amount of risk. After all,

Congressional Oversight Panel

if the risky investment pays off the shareholders reap all the rewards; but if the investment bankrupts the company it is the taxpayers who are left holding the bag.

There are three obvious solutions to the current state of executive compensation: have the government undertake the difficult job of regulating how too big to fail firms pay their workers, end the practice of insuring large firms against failure, or charge firms for the insurance they are being provided. To my way of thinking one of the latter two solutions—ending the government’s too big to fail guarantee or charging firms for the insurance—is the preferred solution, because either is the simplest solution and imposes the least cost on taxpayers. I am well aware that others disagree with my assessment.

Regardless of what one thinks is the optimal solution, I think we can all agree that these issues remain important, and I am interested in hearing what the witnesses have to tell us about the challenges involved in having the government regulate how firms pay their employees, what impact various pay plans could have on employee turnover and the ability of firms to hire skilled workers, and what was accomplished through the efforts of the Special Paymaster. So once again I would like to thank all of the witnesses for agreeing to appear before our panel.

Finally I would like to extend a special welcome to our new chair, Senator Ted Kaufman. For me having Senator Kaufman join us is especially exciting since I am no longer the newest member of the Congressional Oversight Panel. Senator, I want to assure you that I empathize with what you have been going through during the past few weeks trying to catch up on all the fine work the panel has completed. However, burdensome as your work has been, I want know that you are getting off easier than me since the first hearing I participated in was the Panel’s marathon hearing on AIG which lasted for six hours. I am fairly confident that our hearing today will be much shorter.